APPENDIX

Revenue Act of 1926, c. 27, 44 Stat. 9:

> SEC. 302 (as amended by Section 404 of the Revenue Act of 1934, c. 277, 48 Stat. 680). The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside the United States.
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>
> (g) To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent of the excess over $40,000 of the amount receivable by all other beneficiaries as insurance under policies taken out by the decedent upon his own life.
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> * * * * *

Treasury Regulations 80 (1937 ed.):

> ART. 25. *Taxable insurance.*—The statute provides for the inclusion in the gross estate of insurance taken out by the decedent upon his own life, as follows: (a) All insurance receivable by, or for the benefit of, the estate; (b) all other insurance to the extent that it exceeds in the aggregate $40,000.
>
> The term "insurance" refers to life insurance of every description, including death benefits paid by fraternal beneficial societies, operating under the lodge system. Insurance is considered to have been taken out by the decedent, whether or not he made the application, if he acquired the ownership of, or any legal incident thereof in, the policy; but in the case of a decedent

dying before November 7, 1934 (the date of approval of the 1934 edition of Regulations 80), the provisions of the second paragraph of article 25 of Regulations 70 (1929 edition) will continue to apply. Legal incidents of ownership in the policy include, for example: The right of the insured or his estate to its economic benefits, the power to change the beneficiary, to surrender or cancel the policy, to assign it, to revoke an assignment, to pledge it for a loan, or to obtain from the insurer a loan against the surrender value of the policy, etc.

* * * * *

ART. 27. *Insurance receivable by other beneficiaries.*—The statute requires the inclusion in the gross estate of the decedent of the proceeds of any policy, or the aggregate proceeds of all policies, not receivable by or for the benefit of decedent's estate, to the extent that such proceeds exceed $40,000, regardless of when the policy was or the policies were issued, if the decedent possessed at the time of his death any of the legal incidents of ownership.

The estate is entitled to only one exemption of $40,000 upon insurance receivable by beneficiaries other than the estate. For example, if the decedent left life insurance payable to three such beneficiaries in amounts of $10,000, $40,000 and $50,000 (total, $100,000), the full amount should be listed on the return and therefrom subtracted the $40,000 exemption as provided in the appropriate schedule of Form 706. The word "beneficiaries", as used in reference to the $40,000 exemption, means persons entitled to the actual enjoyment of the insurance money.

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No. 244

IN THE

Supreme Court of the United States

OCTOBER TERM, 1945.

AGNES SCHONGALLA, as Executrix of the Last Will and Testament of William Schongalla, deceased,

Petitioner,

vs.

HARRY M. HICKEY, United States Collector of Internal Revenue, Fourteenth District of New York.

On Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

SUPPLEMENTAL BRIEF ON BEHALF OF PETITIONER.

The respondent's brief of approximately 8 1/2 to 9 pages may leave an impression on this Court that this case does not raise any questions of conflict of law between several of the Federal Circuit Courts of Appeal, or any questions of great public importance.

Such, however, is not the case. The case at bar differs in principle from those referred to by the respondent and presents two important questions of law which we seriously contend are unsettled and of great public importance, and which this Court should finally decide.

One of these questions appears to have been misapprehended by the respondent and the other which involves the question of depriving infants of vested interests without giving them their day in court under a misinter-

pretation of a general rule of the common law is mistakenly and perfunctorily dismissed by the respondent as one which "depends upon the facts of this particular case and thus is not of general importance."

On page 7 of respondent's brief it is stated that the cases relied on by petitioner (*Walker v. U. S.; Helvering v. Parker; Bingham v. U. S.;* and *Industrial Trust Company v. U. S.*) were decided several years before this Court's decision in *Helvering v. Hallock*, 309 U. S. 106, which recognized that the retention of rights contingent upon survivorship furnish the basis for the imposition of estate taxes with respect to property *transferred* by the decedent during his lifetime.

In the case at bar we claim that no property was transferred by the decedent during his lifetime and that the taking out of insurance policies by a decedent in favor of designated beneficiaries does not constitute any transfer of property from the decedent in his lifetime.

This is the very point that we are asking this Court in the case at bar to decide and we claim on reason and principle the doctrine of *Helvering v. Hallock* does not apply. The application of the principle of *Helvering v. Hallock* has caused considerable confusion and unjustifiable doubt to be cast on the *Walker, Bingham* and *Industrial Trust Company* decisions which, in reality, unaffected by *Helvering v. Hallock* should control the decision in the case at bar, and which are still, petitioner contends, sound law.

In our case the decedent never had control over the insurance policies and never made or purported to make any transfer of them. Our case squarely places before this Court the opportunity to clear up the confusion caused by *Helvering v. Hallock* in the lower courts as to whether the mere taking out of a life insurance policy

upon an annual premium basis, with a reservation to the insured, of no rights except the possibility of his estate receiving the policy's proceeds if the beneficiary (owner in law) of the policy should by chance predecease the insured, is rendered taxable by reason of such reservation alone where the contingency referred to does not occur.

Helvering v. Hallock may very well apply to cases like *Bailey v. U. S., Commissioner v. Washer,* and *Chase National Bank v. U. S.* (116 Fed. [2d] 625), cited on pages 7 and 8 of respondent's brief, as in each of those cases the insured controlled the policies in his lifetime and then transferred or assigned his control contingently, however, on his own death. A reading of the decisions in those cases and in *Liebmann v. Hassett,* 148 Fed. (2d) 247, demonstrates in our opinion that the Courts, just as respondent's counsel, have failed to perceive that *Helvering v. Hallock* deals with transfers *inter vivos* as taxable under Section 302 (c) of the Revenue Act of 1926, that while an insurance policy may very well be the subject of a transfer just the same as tangible personal property or intangible choses in action, and accordingly taxable under *Helvering v. Hallock* where the transferor retains an interest to inherit upon the death of the transferee preceding his death, nevertheless the principle or theory of *Helvering v. Hallock* does not apply to a mere direction in an insurance policy to pay the proceeds to the insured's estate if the beneficiary predecease him where there has not been and could not be, since the insured had no control over the policy under its terms, any transfer of the policy. The mere taking out of the policy by the insured from the insurance company, under such circumstances, is dealt with in the *Walker, Parker, Bingham* and *Industrial Trust Company* cases, which are in nowise affected in principle by the decision in the *Hallock* case.

The other questions presented by the petitioner are whether a tax-reviewing Court may pass upon matters of general law involving, of necessity, the rights of third parties—in this case infants at the time when insurance policies were taken out, who are named as the beneficiaries in the policies—without giving them their day in court by requiring, as a matter of due process, a trial of the issues involving such rights. This, it is submitted, is a question of enough public importance to be decided by the Supreme Court of the United States, since here the question arises out of the lower Courts themselves raising the issues and then undertaking, after so raising them, to decide them in a proceeding between the United States and the decedent's estate alone, without giving the infants, whose rights are necessarily to be passed upon, their day in court.

In respect to this question, on page 8 of respondent's brief, it is stated:

> "Whether a certain amendment of the insurance policies was properly treated as a reformation does not present a substantial question requiring the intervention of this court."

Will the United States Supreme Court hold that parties may be deprived of vested rights in a tax case to which they are not parties where the Courts decide that an insurance policy may be regarded as reformed and the rights of the beneficiaries adjudicated for tax purposes even though no issue with respect to reformation or to their rights has been with due process of law presented or tried and where they are not before the Court?

Had these infant beneficiaries been represented in any legal proceeding to reform these policies they would have the right that any ordinary human being ought to have, and under our Constitution still has, to produce witnesses and to cross examine them and bring out any evidence

in their favor against a claim that the policies were reformed. Furthermore, the effect and necessary implication of the Circuit Court's decision in this case is that while the beneficiaries of insurance policies may be ultimately liable for the payment of tax thereon under Section 314 (b) of the Revenue Act of 1926, the foundations of their liability may be tried between the government and the estate without proper judicial inquiry being afforded to the beneficiaries.

Such cannot possibly have been the intent of Congress. Is it not incumbent upon a tax-reviewing Court under such circumstances, particularly where the rights of infant beneficiaries are involved, to insist that they have their day in court and the right to a complete examination and cross examination of the evidence rather than to permit the decedent's estate and the government to be the sole contestants and to adjudicate the rights of infants upon evidence not produced on any issue of the infants' rights, but haphazardly applied in the determination thereon?

The question presented by petitioner is not as respondent states—whether a certain amendment of the policies was properly treated as a reformation; that was a conclusory question propounded by the Court itself. The real question submitted by us to this Court is whether the lower Courts, in reviewing the tax liability in the first instance, are not compelled, on being apprised of the existence of collateral issues, upon which the right to tax may depend, to insist upon a trial of those issues and if not tried to refrain from adjudication of them; and, as a corollary, the further question as to whether it is not implied in the Revenue Act that those ultimately liable for taxes on property forming no part of the decedent's legal estate though brought into it for tax purposes, are entitled to judicial inquiry into their rights and liabilities by due process of law, and that where

the adjudication of their rights, as here, becomes manifestly a condition precedent to the determination of their tax liability, the Courts are compelled of their own motion to order and conduct a proper judicial inquiry. The petitioner claims that the insured and the insurance company had no power or authority by agreement between themselves to deprive the infant beneficiaries of vested rights.

For the reasons above given, as well as those contained in our main brief, we pray the Court to grant our application.

Dated: New York, September 20, 1945.

Respectfully submitted,

EDWARD A. ALEXANDER,
Attorney for Petitioner.